

Members of the Board of Education
State Audit Committee
McCracken County Board of Education
Paducah, Kentucky

In planning and performing our audit of the basic financial statements of McCracken County Board of Education, we considered the Board's internal control to determine our auditing procedures for the purpose of expressing an opinion on the financial statements and not to provide assurance on the internal control.

During our audit we became aware of several matters that are opportunities for strengthening internal controls or operating efficiency. We also noted immaterial instances of noncompliance with applicable laws and regulations which we are required to report to you. These comments and recommendations, which have been discussed with the appropriate members of management, are intended to help the Board comply with applicable laws and regulations, improve internal control, and result in other operational efficiencies. The memorandum that accompanies this letter summarizes our comments and suggestions concerning the reportable conditions and other matters.

This report is intended solely for the information and use of the management of McCracken County Board of Education, management, and the Kentucky Department of Education and is not intended to be and should not be used by anyone other than these specified parties.

Kemper CPA Group LLP

Certified Public Accountants and Consultants
Paducah, KY
September 15, 2005

Compliance with State Statues

Comment: Per KRS 160.500, tax collectors are required to submit for deposit all collections which they receive. Fees from collections are required to be billed to the Board separately. Review of County Clerk's collections indicates collections are submitted net of fees. This was noted during the prior year audit.

Recommendation: We recommend the Board request the County Clerk to remit to the Board all school tax collections and submit an invoice for fees related to collection of such taxes.

Comment: Per KRS 160.570, depository funds of the Board and activity funds are required to be fully insured throughout the fiscal year. Deposits, to the extent uninsured by Federal Deposit Insurance Corporation (FDIC), must be collateralized by obligations as permitted by KRS 66.480. We noted activity fund deposits exceeding FDIC coverage which were not collateralized as of year-end. This was noted during the prior year audit.

Recommendation: We recommend the Board obtain collateral agreements with all depository institutions to insure adequate coverage of all funds in excess of FDIC coverage throughout the year.

Other Compliance Matters:

Comment: During our testing of Special Revenue Fund programs, we noted two immaterial instances of unallowable expenditures. During our testing of program 3105, we noted one instance of a computer purchased for administrative purpose when indirect cost allocation was applied. The MUNIS Federal Coding Matrix does not allow purchases of certain equipment for administrative purpose if indirect cost allocations are applied. During our testing of program 3375, we noted an immaterial purchase of cabinets and fixtures for a remodeled room. According to the MUNIS Federal Coding Matrix, remodeling expenditures are not allowable for this program. In addition, we noted several expenditures coded to object code 0690, which is not an appropriate code. For example, we noted computer related expenditures which should have been coded to object code 0734.

Recommendation: We recommend program administrators become familiar with the allowable expenditure requirements and MUNIS Federal Coding Matrix for their programs to insure proper expenditures. The most current version of the coding matrix is easily accessible online at the KDE website.

Other Matters:

Comment: During testing of revenues, we noted instances where daycare receipts were not deposited in a timely manner. Timely deposits of collections results in improved cash flow while reducing the possibility of loss due to theft, fire, or impropriety. This was noted during the prior year audit.

Recommendation: Since the daycare operations are located at various elementary and middle schools, we recommend these operations follow the same guidelines governing activity funds. Collections should be deposited daily unless the amount is less than \$100. Amounts less than \$100, in the aggregate, should be deposited no less than weekly with all funds on hand maintained in a secure area.

Comment: In testing controls over disbursements of the operating account we selected a random sample of 25 disbursements during the year. In addition to the sample selection of disbursements, we obtained the listing of all disbursements during the year and reviewed the activity of significant vendors. This test included approximately 525 individual invoices. Of these selections, we noted the following:

- Three instances of invoices not actually stamped paid, but stapled to a copy of the check as a means of documenting cancellation.
- One instance of a hand issued invoice at the time of service subsequently followed by an invoice received by mail, resulting in duplicate charge for the same service.
- Thirty instances of purchase orders dated after services received. Most of these related to purchases for repairs, maintenance, and reimbursements.
- One instance of purchase order not attached to paid invoice.
- One instance of supporting invoice documentation missing.
- Three instances of immaterial amounts of sale tax paid for hotel and travel expenses. (One instance was an out-of-state hotel not recognizing the Board's tax-exempt status).

These types of weaknesses could result in unauthorized payments and did result in one duplicate payment for \$233, of which, management has requested a refund.

Recommendation: Even though we noted only the one instance of unauthorized payment for \$233 and were able to satisfy ourselves the items selected for testing had been properly received and recorded, we recommend purchase orders be prepared prior to or at the time of service and if this is not possible, documentation of the reason why it is not feasible; supporting documentation maintained for all expenditures; receiving reports, when applicable, be attached to all paid invoices to clearly demonstrate proper controls over the disbursement function. In addition, we recommend all individual paid invoices be clearly stamped paid/canceled to prevent one from becoming detached from the check copy and subject to duplicate payment.

Comment: During our testing of disbursements, we noted the Board does not have a contractual agreement with two vendors who provided services for repairs and maintenance (i.e. concrete work and painting).

Recommendation: The Board was technically not required to bid these services. However, to insure the Board is receiving the highest quality services at the best price, we recommend the Board consider bidding and contracting with vendors which provide such services over an extended period of time.

Comments: Supplies and other items ordered are frequently delivered directly to the various schools with the purchase order and invoice going to the Board's accounts payable department. During our testing of disbursements, we noted several instances where the receiving report was not signed nor initialed indicating the item was received and in the proper condition. To verify proof of receipt the accounts payable clerk presently has to call or email the various schools. Therefore actual proof of receipt is not effectively and efficiently documented which could result in payment for goods not actually received. This was noted during the prior year audit.

Recommendation: We suggest the Board consider developing a central warehouse for receipt of all goods and supplies ordered which would mean there would only be one place where all items are received. Once items received are properly verified by agreeing to shipping documents and purchase orders, such information would be forwarded to the accounts payable clerk.

Comment: Audit entries were required to adjust the balances in the School Food Service Fund accounts receivable and inventory at June 30, 2005. This issue was noted in the prior year management letter.

Recommendations: Again, we recommend the Program director coordinate these matters with the finance director in the future to properly record inventory and receivables in the Board's internally generated financial statements.

Comment: During our testing of Debt Service Funds, we noted revenues from a new bond issue effective in October of 2004 for a partial advance refunding of the 1996 bond series was not recorded. An adjusting journal entry was necessarily made to correct the Debt Service Fund for this bond issue.

Recommendations: We recommend management record these and similar debt transactions.

Comment: In our testing of disbursements, we noted certain expenditures which should have been capitalized were not reflected in fixed asset module. Management had also noted several unrecorded additions to actual inventory of fixed assets while performing annual physical review of fixed assets at various schools. In testing various expenditures, we also noted additional improvements which were not reflected in the fixed asset module.

Recommendation: We recommend management closely monitor expenditures which meet the requirements for capitalization throughout the year and pass this information to the fixed asset director for follow-up to determine if these expenditures do meet the criteria for capitalization.

Comment: During our testing of capital assets and inspection of the warehouse, we noted a separate area has not been designated and secured for the receipt of capital assets. As there are times when the warehouse is open and easily accessible, unsecured capital assets are subject to misappropriation. In addition, we noted the Board was in the process of upgrading the District's network and scrapped technology related capital assets were intermingled with new technology related assets in the warehouse, which increases potential for scrapping new assets.

Recommendation: Conversations with management indicated all assets subject to disposal are individually inspected and approved prior to disposal. However, with the warehouse easily accessible to the public, we recommend securing an area of the warehouse for storage of new capital assets until they are properly verified and placed in service. This would help prevent possible misappropriation, as well as, inadvertently disposing of a new asset with scrapped assets.

Comment: Conversation with management indicated physical inventories of capital assets at each of the District's various locations were not performed during the year. During the current year, physical inventories were performed at approximately half of the District's locations.

Recommendation: Capital asset expenditures may occur in various object codes. Unless notified, such purchases may not be tagged and updated in the fixed asset module by the fixed asset manager. We recommend management closely monitor expenditures that may meet the requirements for capitalization throughout the year and pass this information to the fixed asset manager for follow-up to determine if these expenditures do meet the criteria for capitalization.

However, relying on review of expenditures will not insure recording of all asset additions and disposals within the fixed asset module. Annual physical inventories of fixed assets should be performed at all locations to insure proper updating of the fixed asset module and investigation of any variances noted during the inventories.

Comment: During our testing of fixed assets, we noted the balances reflected in the fixed asset module of the MUNIS system were not reconciled with the MUNIS general ledger during the year. Adjusting journal entries were necessarily made to correct the MUNIS general ledger.

Recommendations: In order to truly reconcile the fixed asset module of the MUNIS system to the general ledger, we recommend management export the active assets from the fixed asset module to an excel spreadsheet; sort the listing by class; and verify the historical cost and accumulated depreciation agrees with the general ledger for funds 80, 81 and 82. Any variances should be investigated and the cause for variance determined before adjusting as necessary to insure the MUNIS general ledger reconciles with the fixed asset module.

Comment: During our testing of capital assets, we noted the District does not have a formal means of identifying and recording donated capital assets. Most donated additions come from various support organizations (i.e. Boosters, Parent-Teacher Organizations, etc.). Significant donations generally are presented to the Board of Directors for approval (i.e. installation of sport field lighting, approval of construction, etc.) and are easily identified. However, some assets, such as playground equipment, may be donated directly to a school without the fixed asset manager's knowledge. In reviewing the District's minutes, we noted several donations, of which, two required capitalization. Without identifying these donations as capital expenditures in the fixed asset detail records, the District is at risk of not having adequate insurance to cover these improvements.

Recommendation: We recommend management develop procedures to identify and record donated assets. These procedures should require the support and input from the principals and director of facilities to insure all donated fixed assets are properly recorded.